

Report of the auditor-general to the Mpumalanga Provincial Legislature and the council on the City of Mbombela Local Municipality

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the City of Mbombela Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2019, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget and actual amounts for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the possible effects of the matter described in the basis for qualified opinion section of this auditor's report, the financial statements present fairly, in all material respects, the financial position of the City of Mbombela Local Municipality as at 30 June 2019, and its financial performance and cash flows for the year then ended in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act, 2018 (Act No. 1 of 2018) (Dora).

Basis for qualified opinion

Cash and cash equivalents

3. I identified unreconciled differences between the cash book and the bank statement balance that could not be supported by sufficient and appropriate evidence. The municipality did not have adequate systems in place to maintain records of cash and cash equivalents. I could not confirm the cash and cash equivalents by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to cash and cash equivalents disclosed in note 9 to the financial statements, stated at R126 050 714 in the financial statements.

Context for the opinion

4. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of this auditor's report.

5. I am independent of the municipality in accordance with sections 290 and 291 of the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* and parts 1 and 3 of the International Ethics Standards Board for Accountants' *International code of ethics for professional accountants (including International Independence Standards)* (IESBA codes) as well as the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA codes.
6. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Material uncertainty relating to going concern

7. I draw attention to the matter below. My opinion is not modified in respect of this matter.
8. I draw attention to note 63 to the financial statements, which indicates that the municipality incurred a net loss of R199 583 167 (2017-18: R210 656 766) during the year ended 30 June 2019 and, as of that date, the municipality's current liabilities exceeded its current assets by R1 513 885 585 (2017-18: R1 335 923 723). As stated in note 63, these events or conditions, along with other matters as set forth in note 63, indicate that a material uncertainty exists that may cast significant doubt on the financial sustainability of the municipality.

Emphasis of matters

9. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Restatement of corresponding figures

10. As disclosed in note 50 to the financial statements, the corresponding figures for 30 June 2018 were restated as a result of errors in the financial statements of the municipality at, and for the year ended, 30 June 2019.

Events after reporting date

11. As disclosed in note 65 to the financial statements, grant funding amounting to R101,8 million was not approved for rollover by the National Treasury.

Unauthorised expenditure

12. As disclosed in note 58 to the financial statements, the municipality incurred unauthorised expenditure of R267 153 091, due to overspending of the approved operational budget.

Fruitless and wasteful expenditure

13. As disclosed in note 59 to the financial statements, the municipality incurred fruitless and wasteful expenditure of R38 041 859, due to interest charges on overdue accounts.

Irregular expenditure

14. As disclosed in note 60 to the financial statements, the municipality incurred irregular expenditure of R208 935 017, as it did not follow proper procurement and contract management processes.

Material impairments – trade receivables

15. As disclosed in notes 5 and 7 to the financial statements, the receivables balance was significantly impaired. The total impairment of receivables amounted to R216 025 282 (2017-18: R327 255 103), which represented 43% (2017-18: 58%) of the total receivables. As disclosed in note 43, actual bad debts of R243 757 993 (2017-18: R252 693 799) were written off.

Material losses – electricity

16. As disclosed in note 56 to the financial statements, material electricity losses of R121 604 570 (2017-18: R106 030 614) were incurred, which represented 17,12% (2017-18: 16%) of the total electricity purchased.

Material losses – water

17. As disclosed in note 56 to the financial statements, material water losses of R6 955 440 (2017-18: R4 731 946) were incurred, which represented 25,20% (2017-18: 20,50%) of the total water pumped.

Other matter

18. I draw attention to the matter below. My opinion is not modified in respect of this matter.

Unaudited disclosure note

19. In terms of section 125(2)(e) of the MFMA, the municipality is required to disclose particulars of non-compliance with the MFMA in the financial statements. This disclosure requirement did not form part of the audit of the financial statements and, accordingly, I do not express an opinion on it.

Responsibilities of the accounting officer for the financial statements

20. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the SA Standards of GRAP and the requirements of the MFMA and Dora, and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.
21. In preparing the financial statements, the accounting officer is responsible for assessing the municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the appropriate governance structure either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the financial statements

22. My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.
23. A further description of my responsibilities for the audit of the financial statements is included in the annexure to this auditor's report.

Report on the audit of the annual performance report

Introduction and scope

24. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
25. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators/measures included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.

26. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected development priorities presented in the annual performance report of the municipality for the year ended 30 June 2019:

Development priorities	Pages in annual performance report
Water supply	xx – xx
Sanitation	xx – xx
Electricity supply and energy management	xx – xx
Roads infrastructure development and storm water	xx – xx
Public transport	xx – xx
Rural development	xx – xx
Waste and environmental management	xx – xx

27. I performed procedures to determine whether the reported performance information was properly presented and whether performance was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
28. I did not raise any material findings on the usefulness and reliability of the reported performance information for these development priorities:
- Water supply
 - Sanitation
 - Electricity supply and energy management
 - Roads infrastructure development and storm water
 - Public transport
 - Rural development
 - Waste and environmental management

Other matters

29. I draw attention to the matters below.

Achievement of planned targets

30. Refer to the annual performance report on pages xx to xx for information on the achievement of planned targets for the year.

Adjustment of material misstatements

31. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of water supply, sanitation, electricity supply and energy management, roads infrastructure development and storm water, and public transport. As management subsequently corrected the misstatements, I did not raise any material findings on the usefulness and reliability of the reported performance information.

<h2>Report on the audit of compliance with legislation</h2>
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Introduction and scope

32. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.
33. The material findings on compliance with specific matters in key legislation are as follows:

Annual financial statements, performance reports and annual reports

34. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements in the cash flow statement and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected, but the supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.

Expenditure management

35. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
36. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R267 153 091, as disclosed in note 58 to the financial statements, in contravention of section 62(1)(d) of the MFMA. All of the unauthorised expenditure was caused by overspending of the operational budget.

37. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R38 041 859, as disclosed in note 59 to the financial statements, in contravention of section 62(1)(d) of the MFMA. All of the disclosed fruitless and wasteful expenditure was caused by interest charged on overdue trade payables.
38. Reasonable steps were not taken to prevent irregular expenditure amounting to R208 935 017, as disclosed in note 60 to the financial statements, as required by section 62(1)(d) of the MFMA. The majority of the irregular expenditure was caused by procuring services through the extension of contracts, deviating from normal procurement processes and participating in awards by other organs of state rather than by inviting competitive bids.

Procurement and contract management

39. Some of the goods and services with a transaction value above R200 000 were procured without inviting competitive bids, as required by supply chain management (SCM) regulation 19(a), but rather through multiple extensions of contracts and deviations from normal supply chain processes. Similar non-compliance was also reported in the prior year.
40. Some of the invitations for competitive bidding were not advertised for the required minimum period, in contravention of SCM regulation 22(1) and 22(2). This non-compliance was identified in the current year relating to the procurement processes for the appointment of consultants in the 2015-16 financial year.
41. Measures to combat the abuse of the SCM system were not implemented as per the requirements of SCM regulation 38(1). This related to instances identified in the current year relating to a prior year, as some contracts were awarded in the 2015-16 financial year to providers who had failed to disclose if they had been convicted of fraud or corruption during the previous five years.

Consequence management

42. Cases of financial misconduct that constitutes a crime committed by officials were not always reported to the South African Police Service, as required by municipal regulation on financial misconduct procedures and criminal proceedings 10(1).

<h3>Other information</h3>

43. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report. The other information does not include the financial statements, the auditor's report and those selected development priorities presented in the annual performance report that have been specifically reported on in this auditor's report.
44. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.

45. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected development priorities presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
46. I have nothing to report in this regard.

Internal control deficiencies

47. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance on it. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the qualified opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.
48. Recording, reviewing and reporting processes and controls over current assets and disclosure notes in the financial statements were not adequate.
49. The municipality did not have sufficient monitoring controls to prevent unauthorised, irregular as well as fruitless and wasteful expenditure.
50. Non-compliance with legislation could have been prevented had compliance been properly reviewed and monitored.

Auditor-General

Mbombela

30 November 2019



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence

Annexure – Auditor-general's responsibility for the audit

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements, and the procedures performed on reported performance information for selected development priorities and on the municipality's compliance with respect to the selected subject matters.

Financial statements

2. In addition to my responsibility for the audit of the financial statements as described in this auditor's report, I also:
 - identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control
 - obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control
 - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer
 - conclude on the appropriateness of the accounting officer's use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the municipality's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of this auditor's report. However, future events or conditions may cause a municipality to cease continuing as a going concern
 - evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation

Communication with those charged with governance

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.
4. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and, where applicable, related safeguards.